Amendment In Delisting Regulations: Axing The Minority Rights

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Editor's Notes: *SEBI (Delisting of Equity Shares) Regulations, 2009 provide exit opportunity to existing shareholders when the company seeks to delist its equity shares from stock exchanges – such opportunity is necessary as 'listing' carries an inherent feature of 'liquidity' which gets curbed when the shares are 'delisted'.*

Facilitating smooth implementation of IBC called for supportive amendments in various SEBI regulations, including the delisting regulations. The amendment calls for inapplicability of the regulations where delisting is done pursuant to a resolution plan approved under IBC – this, however, is subject to the condition that the public shareholders get exit price which shall not be less than the liquidation value.

The note below studies if this is at all a fair deal for the minority shareholders.

A protective framework for minority shareholders ensures a robust and dynamic secondary market for securities. As such, the laws shall aim shielding the rights of minority shareholders in disadvantageous circumstances, ensuring that the market is safe and that the possibilities of them losing out on their monies is unlikely except when the market goes red. This holds true as conventional wisdom and as such, there should have been no exceptions while facilitating implementation of the Code.

Magical resolution plans?

However, the regulators seem to have relied on the magic of resolution plans framed under IBC so much so that in one of the Circulars [October, 2017], the Ministry of Corporate Affairs clarified that the approval of the shareholders of the corporate debtor for a particular action required in the resolution plan for its implementation, which would have been required under Companies Act, 2013 or any other law if the resolution plan was not being considered under IBC, is *deemed to have been given* on its approval by the adjudicating authority [i.e. NCLT].

Endorsing the above, SEBI came up with a Discussion Paper [March, 2018], soliciting views on compliance requirements by listed entities undergoing corporate insolvency resolution process under IBC. The Discussion Paper, among other things, proposed relaxations in the provisions of the LODR Regulations, 2015 as well as the Delisting Regulations, 2009.

The notion of an *all-pervasive all binding* resolution plan is based on section 31 of IBC which says that a resolution plan approved by NCLT shall be binding on the corporate debtor and its employees, members, creditors, guarantors and other stakeholders involved in the resolution plan. The conclusion arrived at by the regulators fails to appreciate that resolution plan, though a statutory plan, is substantially a contract between the financial creditors, the existing promoters, and the potential acquirer of the corporate debtor. All others, *viz.* operational creditors and minority shareholders are merely spectators bound by the resolution plan. Section 30 (2) of IBC provides for

repayment of liquidation value due to operational creditors and to dissenting financial creditors; however, is completely silent on the rights of minority shareholders.

Amendment in Delisting Regulations

The Delisting Regulations regulates the conditions under which, and the procedure by which, it is possible to delist the securities of a listed entity. The delisting regulations provide for an exit opportunity for existing shareholders at a price determined through reverse book building process. The reason behind providing this exit opportunity at a market-determined price is simple – the investments which the existing shareholders hold in liquid form will become illiquid once the shares are delisted; hence, leaving the shareholders with no option but to tender their shareholdings at whatever price being offered to them by principal shareholders. The exit opportunity ensures a fair bargain for the minority shareholders.

SEBI, recently *vide* SEBI (Delisting of Equity Shares) (Amendment) Regulations, 2018 ["the amendment"], has amended the delisting regulations to provide that these regulations shall not apply to any delisting of equity shares of a listed entity made pursuant to a resolution plan approved under IBC, provided *any of* the following 2 conditions are fulfilled –

- The resolution plan lays down specific procedure to complete the delisting; ***or***
- The resolution plan provides exit opportunity to the existing public shareholders at a specified price, which ***shall not be less than the liquidation value*** ascribed in accordance with section 53 of IBC. However, where existing promoters/any of the shareholders, whether directly or directly, are allowed exit at a higher price (i.e. higher than the liquidation value), the public shareholders shall receive no less.

The Amendment assures the public shareholders of getting a minimum of liquidation value where the corporate debtor is sought to be delisted pursuant to a resolution plan. Interestingly, the expression "liquidation value to equity-holders" sounds like an oxymoron in the context of insolvent liquidations.

Fruits of the amendment? One positive effect is easing out the process for the acquirers; however, the news might not be so good for the minority shareholders.

The liquidation value assurance: a careless concern

The amendment assures the public shareholders of getting a minimum of *liquidation value* where the corporate debtor is sought to be delisted pursuant to a resolution plan. Interestingly, the expression "*liquidation value to equity-holders*" sounds like an oxymoron in the context of *insolvent liquidations*. Had there been a liquidation value attributable to equity-holders, there would have been no question of insolvency. A positive liquidation value to equity-holders implies that there is enough for the debt-holders to have their dues paid off. So, where is the insolvency?

That makes it clear - one can expect nothing but erosion of value in the hands of minority shareholders. Liquidation value attributable to an equity-holder in an insolvent entity, in usual cases, would not be more than *nil*. Consequentially, the market value of the public shareholding comes down to *zero.* Hence, the exit opportunity at liquidation value is not even a deal for minority.So, where is the minority protection? Unfortunately, it seems to have lost in the amendment.

Minority to be blamed?

A point often in argument is when a company goes insolvent, the creditors take control and that the equity-holders should take a backseat. So, classification as a principal shareholder or as a minority shareholder is irrelevant.

The amendment seeks to equalize the exit value available to minority shareholders with the exit value offered to principal shareholders. The amendment says where the existing promoters or any other shareholders are provided an opportunity to exit at better prices, the existing public shareholders shall also be provided exit opportunity at least at the same price. In liquidations under IBC, promoters' equity being written off is not uncommon. Hence, the utility of this provision in safeguarding the worth of minority shareholders' investments is questionable.

Besides, this idea of keeping a principal shareholder and a minority shareholder at the same pedestal seems to neglect the very fact that minority shareholders have negligible say in the business decisions of the entity, even if they exercise their right to vote. So, the eventuality of a principal shareholder not getting anything shall not preclude a minority shareholder from receiving his paper's worth. The position of a minority shareholder in resolution process is no better than an operational creditor – no opportunity of being heard, no representation in the decision-making body, and yet bound by whatever has been decided by a completely different set of stakeholders.

It may be noted that similar exemption was there for schemes framed under BIFR regime, if the scheme provided an exit option to the existing public shareholders at a specified rate. The intent was clear, that is, protection of the rights of minority shareholders. Notably, there was no concept of "liquidation value" during BIFR regime. This is evident of the underlying objective of such regulations – where an entity is sought to be delisted, those not agreeing to such delisting should be allowed to disagree (and therefore, exit), by taking their fair share.

What's the solution?

Regulatory dicta like these seem to turn a Nelson's eye to the basic tenets of law-making including principles of natural justice; and fundamental democratic set-up of company law. The fallacy of guaranteed liquidation values during the resolution phase might not work well in serving the interests of those who have not been parties to the resolution plan. The big question is regarding determination of the value of the minority shareholding. The answer probably lies in the difference between the fair value of the entity and the total debts.

There was definitely a need for amending the delisting regulations and making things easier for the acquirer; however, it is to be ensured that the same does not send negative ripples across the secondary market.